

COST *and* MANAGEMENT

THE OFFICIAL JOURNAL OF

THE SOCIETY OF

INDUSTRIAL AND COST ACCOUNTANTS OF CANADA

Telephone 2-0700

INCORPORATED 1920

HEADQUARTERS: 601-602 MACKAY BUILDING,
66 KING STREET EAST, HAMILTON

J. N. Allan, R.I.A., Secretary-Manager and Editor

VOL. XXII

JUNE

No. 6

.. CONTENTS ..



EDITORIAL	202
CHAPTER NOTES	204
NEW MEMBERS	207
CURRENT LITERATURE DIGEST	208
REPORT WRITING	214
THE BASIS FOR ADEQUATE FINANCIAL REPORTING	221
THE BALANCE SHEET FROM THE BANKER'S VIEWPOINT	225
ACCOUNTS PAYABLE PROCEDURES	228



Subscription price to non-members, \$5 per year. Single copies, 50 cents.
Members desiring five copies or more of a single issue may obtain them at
25 cents each. Authorized as second class mail, Post Office Department,

Ottawa.

• EDITORIAL •

The Accountant and The Lawyer Get Together

Over the years as government regulation and taxation have played a larger and larger part in our business affairs, the accountant's job has become correspondingly more complex. In the old days, it was enough for the accountant to have accounting theory at his fingertips and to be guided by it in handling most of his business problems. Now he must be an expert on many other things in addition to his accounting skill.

The Income Tax Act has probably been the source of most of the accountant's added problems. It has made great inroads into earlier methods of handling accounting problems. Some time ago, it reached the point in importance and complexity where many companies began to treat it primarily as a legal problem. This, of course, it necessarily is when any important points of difference arise between a company's accounting division and the Income Tax Department. Many companies, however, have continued to handle tax matters as almost purely an accounting function. Among smaller companies this is a matter of necessity. It has the disadvantage, however, of placing the accountant in the position where, if he is uncertain about some Income Tax matter, he is prone to ask the Income Tax Department for a ruling. In thus referring to the other fellow for decisions he may be passing up opportunities to get more favourable results by taking a stand which a legal man might know to be within his rights under the Act.

The point seems to arise from all of these circumstances that Income Tax problems are neither solely accounting nor solely legal in nature, but a delicate combination of both. As a result, it is one of those situations which calls for a very high degree of co-operation between the two professions if the best results are to be achieved. This will be even more necessary under the terms of the New Income Tax Act, which it is expected will be enacted this year, since under its provisions, it is expected that accepted accounting procedure will carry more weight in establishing tax procedure than under the old act. This feature, and the provision for an Income Tax Court of Revision tie the legal and accounting professions together almost inextricably insofar as income tax matters are concerned. Sales Tax and many other government regulations are somewhat in the same category.

It would appear then that if we are to place our companies in as strong a position as possible with respect to taxation and regulation, we of the accounting profession must co-operate "across the board" with the legal profession. This means, as far as larger companies are concerned, that a close and harmonious condition should exist between accounting and

EDITORIAL

legal departments. The accounting division of smaller companies with no legal department must, of course, perform a semi-legal function in these matters, but might also do well to get competent legal help periodically, rather than rely too heavily on Tax Department rulings.

Professor McDougall on Income Tax

On May 27th, Professor J. L. McDougall, of Queen's University, told a meeting of the Canadian Manufacturers' Association that in his opinion continued high income tax was an unwise policy, but spoke in defense of the sales tax. Although most of his remarks were centred around the personal income tax the same reasoning can be applied to corporation income tax, and we presume that Professor McDougall intended that this be done. He stated that if income taxes were kept as low as possible, and Sales Tax relied on for a larger part of governmental income, the individual (to which we add the corporation) would get what he earned, and he was free to exercise his judgment as to what purchases he made of goods that were subject to sales tax. It is indeed cheering to hear of an economics expert taking up the cudgels to beat down income taxes.

The Dominion Budget, 1948

The Dominion Budget Resolutions submitted to parliament by the Minister of Finance on May 18th contained no astounding surprises, although perhaps a few disappointments.

No change was made in Corporation Taxes. The minister stated that the present rate, together with the provincial tax is slightly lower than that of the United States, and seemed to be yielding satisfactory net profits to corporations.

More news came out about the New Income Tax Act. It is now expected that it will be introduced again as soon as the Budget Resolutions have been dealt with. It is now proposed that the New Act will be effective January 1st, 1949, instead of 1948. This will save a lot of head-scratching over retroactive adjustments. It is expected that there will be some minor changes in the present Income War Tax Act effective in 1948.

On the whole, business and industry in general will not suffer much from the proposed budget legislation, but conversely they cannot be said to have gained much.

Chapter Notes

BAY OF QUINTE

The closing meeting for the season was held at the Bar B-Q Tavern Restaurant on Monday, May 10th. Guests were welcomed from the Kingston and Peterborough Chapters by our Chairman, Harold Kellar. Mr. W. G. Leonard and Mr. R. C. Bastable, respective Chairmen of the visiting Chapters, responded and emphasized the good will and good fellowship resulting from inter-chapter meetings and it was their earnest desire to continue and co-operate in joint meetings.

One of the original members of our Chapter, Mr. Les Lennox, was the speaker of the evening and chose as his subject, "The Cost Accountant's Role in Industry." He centred his talk about the following three headings: 1. Cost Control; 2. Cost Reporting and 3. Cost Analysis.

At the close of this interesting address, Gordon Ireland thanked the speaker on behalf of the Chapter.

Election of Directors for the coming year were held and the Scrutineers' report was as follows: C. J. Casey, E. E. Tummon, A. Lockley, D. R. Duffy.

Bob Taylor was re-appointed Secretary-Treasurer for the coming year.

Harold Kellar congratulated the new directors and thanked the retiring executive and committee chairmen for their efficient co-operation during the past year. Les Lennox voiced the members' appreciation of the retiring executive.

Subjects voted high priority for the talks for the coming season were General Accounting, Cost Accounting, Budgets, Income Tax and Time Study.

The social portion of the meeting commenced at 9.15.

EDMONTON

At the beginning of the year just concluded it was decided to depart from the lecture program followed by the Chapter during the past few years. It was felt that more active participation of the members in the program would have a stimulating effect on the membership as a whole and would also provide a means of studying accounting methods in use in the various businesses represented within the Chapter. The result of this program was a series of most interesting lectures, ably presented by the members concerned, on accounting methods peculiar to their particular line of business. The subjects covered and names of the speakers are listed and give a very good indication of the interesting material covered during the year:

Budgetary Control—Wholesale Accounting—Mr. Lee Dallison.

Dominion Income Tax Aspects—Mr. Gordon Northfield.

Public Utility Consumer Accounting Records—Mr. Jack Cummings.

Depletion Allowance in the Coal Mining Industry—Mr. Fred Mitchell.

Cost Accounting in Steel Fabrication Plants—Mr. Wm. McKinnon.

The Meat Packing Industry—Mr. Gordon Perring.

Telephone Accounting Records—Mr. Roland Wood.

CHAPTER NOTES

In addition to those given by members, five very interesting lectures were presented by guest speakers on a variety of subjects covering matters of particular interest to the chapter members.

Although the practice of having the Chapter members prepare and present a good proportion of the talks during the year may not be a particularly novel one, it did nevertheless create a new interest and amply justified its introduction.

FORT WILLIAM-PORT ARTHUR

The Annual Meeting of the Fort William-Port Arthur Chapter was held at the Port Arthur Casino, Friday, May 28th with 27 members and one guest present. The Chairman, Mr. R. B. LeCocq, presided.

The Chairman reported on the year's activities and after a discussion on several features of the year's activities, it was moved by Mr. R. K. Piper and seconded by Mr. C. W. King and unanimously carried that the sincere thanks and appreciation of all members of the local chapter be extended to our retiring Chairman, Mr. LeCocq, for his continuous and energetic efforts as Chairman for the last two years.

The Directors elected as their officers the following: Chairman, James A. Aitken; Vice-Chairman, C. D. Henderson; Secretary-Treasurer, Leslie D. Dack.

HAMILTON

Hamilton Chapter's closing dinner meeting on May 20th was its annual business meeting without frills or speaker.

The previous year was frankly reviewed, and plans for the coming year were discussed and adopted. An active and profitable year appears to be ahead.

The election of officers resulted as follows: Chairman, W. C. Sparham, R.I.A.; 1st Vice-Chairman, W. R. Spence; 2nd Vice-Chairman, J. Crossan, C.A.; Secretary-Treasurer, A. R. Wright, R.I.A.

Owing to the onerous duties imposed on the Secretary-Treasurer, J. Bracewell, R.I.A., was elected Assistant Treasurer.

The Immediate Past Chairman, Harold Bricker, R.I.A., installed the newly elected officers.

KINGSTON

On May 20th the Kingston Chapter held their final dinner meeting of the season at the LaSalle Hotel. The guest speaker of the evening was Mr. K. G. Crawford, Director of the Institute of Local Government at Queen's University who spoke on taxation as applied to business and brought out some very interesting viewpoints in this connection, particularly the fact that industry like individuals enjoyed many services which added greatly to the facilities of such enterprises. Not only did Mr. Crawford handle his subject with great skill but he also proved to be a wit and a humorist and a past master at repartee which he directed to his introducer, Mr. Alex Taylor. He was ably thanked by Mr. D. Dalgleish.

COST AND MANAGEMENT

At the same meeting the following directors were elected for the 1948-49 season and on Tuesday, 25th May, these directors were appointed as follows:

Chairman, G. E. Carson; Past Chairman, W. G. Leonard; Vice-Chairman, L. C. McKnight; Secretary-Treasurer, D. Dalgleish; Membership, F. Dane; Programme, R. G. Neill, A. Taylor; Transportation, K. B. Jackson; Publicity, E. Johnson; Educational, J. G. Hall.

LETHBRIDGE

At a meeting of the executive held on May 13th at the home of Mel Parkyn, Chairman, the following officers were elected and committees appointed for the year 1948-49:

Chairman, J. Lakie; Vice-Chairman, J. Craine; Secretary-Treasurer, W. T. Hurst. Committees—Program: Jack Craine, Chairman, Mel Parkyn, Don Brownrigg, Jack Kimber; Membership: Harvey Greenway, Chairman, Bill Hurst, Bert Leys, Ken Barnett; Publicity: Mel Parkyn; Students Advisory: Arthur Brown, Chairman, Vern Wark; Fellowship: Cliff Jones, Chairman, G. Ireson, Wilf Shreeve; Attendance: Bill Hurst, Allan Thompson; Provincial Council: Don Brownrigg; Librarian: Arthur Brown.

At our regular meeting held on the 27th of May after the close of general business, a discussion followed on the topic of "Inventories" led by Jack Craine. The discussion proved a very interesting one to those attending the meeting. The subject of inventories as relating to the various types of industries were discussed by the following members taking part, Jack Craine, Jack Lakie, Don Brownrigg, Arthur Brown and Harvey Greenway.

We are looking forward to more discussions of this nature in the future.

MONTREAL

The Annual General Meeting of the Montreal Chapter was held May 14th when a good number of members turned out to hear reports of the season's activities and to elect a new Board of Directors. The new Directors held a short meeting to elect their officers and the following will serve for the ensuing year:

Chairman, M. H. Bacon; 1st Vice-Chairman, A. S. Keiller; 2nd Vice-Chairman, F. W. Naylor; Secretary, W. G. Joule; Treasurer, L. Bolduc.

A roll of movie film was shown by Gordon Mock, of last year's trip to Fort William to attend the Annual Meeting. Fred Naylor and Arthur Andrews combined to show two reels of talkies which brought the meeting and the season to a conclusion. A presentation was made to our retiring Chairman, Mr. A. V. Harris, in recognition of his efforts throughout the past season.

NIAGARA

The final meeting of the Niagara Chapter was held in the Welland House on Wednesday, May 19th.

Chairman, A. M. Chesher, presided and duly installed the following officers for the 1948-1949 season:

Chairman, J. W. Shea; Vice-Chairman, D. B. Jones; Secretary-Treasurer, Alfred Owen; Directors, C. I. Little, L. Neal, F. H. Hesler,

CHAPTER NOTES

J. E. Thorpe, J. A. Skidmore, F. E. Poynton, S. G. Cherrie, H. R. White,
J. S. McLaren, A. M. Chesher.

OTTAWA CHAPTER

The Annual Meeting of the Ottawa Chapter was held in the cafeteria of the E. B. Eddy Co. on Thursday evening, May 20th.

The following directors were elected for the year 1948-49:

Chairman, C. B. Watt, R.I.A.; Vice-Chairman, P. J. Nolan; Secretary, B. H. Breckenridge; Treasurer, G. S. Olsen; Programs and Meetings, D. R. Hutton, James C. Scott, G. S. Malloch, R.I.A.; Education, A. A. Stearns, M.A., B.C., B.H.D.; Membership and Students, Miss D. Craig; Publicity and Public Relations, Major R. B. Strange, E.D., R.I.A., F.A.E.

After the close of financial business and the election, a panel discussion on costing problems of the present day was held. This brought out some very interesting ideas and arguments. Everyone had an opportunity to express ideas and did so very freely.

Major R. B. Strange thanked the members of the panel, A. A. Stearns, B. H. Breckenridge and Don McAllister, for a very interesting presentation of the subjects.

TORONTO

The final meeting of the Toronto Chapter for the 1947-48 season was a Ladies' Night held at the "Old Mill." The large group gathered in the Garrett Room for cocktails and for introductions to new members and friends and for the renewing of old friendships. The dinner was a very cheerful occasion with large friendly groups joined at tables and the speech-making limited to a minimum. Following the dinner, dancing was enjoyed until closing.

The Toronto Chapter was favoured to have as guests at this meeting, many out of town members. It is indeed unfortunate that such evenings cannot be held more frequently.

New Members

Hamilton Chapter

John Benford, Dominion Foundries & Steel Co. Ltd.

London Chapter

George S. Bean, Silverwood Dairies Ltd.

Gordon H. White, Silverwood Dairies Ltd.

Peterborough Chapter

K. W. Bolam, Dominion Woollens & Worsted, Ltd.

S. J. Richardson, Canadian General Electric Co. Ltd.

G. R. Pulkinghorn, Canadian General Electric Co. Ltd.

L. H. Bearne, Outboard Marine & Mfg. Co. of Canada Ltd.

Toronto Chapter

John S. Grant, C.A., Peat, Marwick, Mitchell & Co.

Winnipeg Chapter

C. F. Lidster, Winnipeg Electric Co. Ltd.

T. B. Milne, Great West Life Assurance Co.

Current Literature Digest

By HAROLD BRICKER, C.G.A., R.I.A.

The European Recovery Assistance is one of the current topics of the day. The economic effect appears to be the greatest concern. However, the Journal of Accountancy, 85-5-392, published an article suggesting the administration with a "businesslike" organization for supervision. There will be, as in government operations, fiscal and accounting responsibilities.

One of the first problems will be to select and obtain the services of personnel qualified to assume the responsibilities to be assigned. Such persons are not generally found in the government staff and in order that a balanced organization that will function along businesslike principles may be formed, it would seem that business will have to loan, not only top administrators, but many financial, accounting, and cost accounting technicians and controllers, to build up the staff to carry out the operation quickly and efficiently, to provide the executive caliber required, as indicated by the appraisal of the whole program. It is a case of getting the men for the job rather than assigning the job to the available men, as may be appreciated in the following factual conditions:

1. Congress and the American people want a businesslike administration of the Marshall Plan.
2. The law permits the establishment of a flexible, businesslike organization.
3. The organization established should not follow the accepted pattern of government agencies, which usually do not emphasize fiscal control.
4. The major fiscal control problem confronting the new agency will be the development of prompt and accurate fiscal information and the use of this information before and during operations, rather than after decisions have been made.
5. Fiscal control can best be secured by establishing a Controller and Fiscal Control Unit of the administration's office, with complete authority over all fiscal reports, records and analysis.

If the Controller is not capable or negligent in his functioning, he can become a bottleneck. Further to this is the fact that any control or co-ordination point may also become a bottleneck if it does not perform the work.

There is probably no peacetime enterprise whose world scope may be for good more directly, to more humanity, than the E.R.A. It would be too bad if it failed through faulty administration due to the lack of qualified personnel.

AN INVESTIGATION OF THE USES OF STANDARD COSTS

The Journal of Accountancy, 85-5-402, summarized a basic study of this problem by Raymend P. Marple, Ph.D., C.P.A., Asst. Sec. N.A.C.A., which may permit a repeat on this subject.

CURRENT LITERATURE DIGEST

Due to rapidly changing world economic conditions and international trade relationships, it sometimes, for various types of business, appears questionable whether standard costs, in their present use, are functioning according to the purpose for which they were originally designed.

The historical cost gave way to standard cost some years ago. In time these standard costs were incorporated into the accounts and used to cost production. The development of predetermined overhead rates designed to obtain full absorption of fixed costs at a normal rate of activity also contributed to the present-day concept of standard costs. With the further development of standard costs, cost accounting became a valuable tool with management, which they used in the control of direct costs. Then, the flexible budget extended this control to indirect costs.

Actual costs can never be kept exactly in line with standard costs. The variances require some forecasting for budget purposes. The need and amounts of the anticipated variance will depend on the level at which the standards were set. Where both the standards and the budgets are based on attainable performances, and where the standards are current, the variances are likely to be relatively small.

Standard costs are more useful for pricing purposes than actual costs, for the following reasons:

1. Being based on carefully determined usages of material and labor, they do not include the accidental distortions caused by excess spoilage, reoperations, etc. To the extent that these excess costs are avoidable by competitors, they are probably not recoverable in selling prices.
2. Adjustments of standard costs to reflect changes in material prices and labor rates are easily made because of the separate price and quantity standards.
3. Standard overhead rates based on normal activity levels provide an acceptable base for prices which will provide for full recovery of overhead costs in the long run.
4. Standards provide a practical method of assigning marketing costs to products to obtain complete production costs.

For those who are not yet operating on standard costs it might not be fully appreciated that the use of standard costs saves clerical expense by eliminating the detailed record keeping necessary for actual costs. Expenses are reduced by:

1. Keeping stock ledgers in terms of quantities only.
2. Pricing and extending requisitions and bills of materials at a uniform standard in place of the computed actual cost.
3. Computing cost of goods finished by extension of quantities at standard.
4. More timely issuance of reports.
5. Saving of executive time through reports based on the principle of exceptions.
6. Saving time in the assembling of costs for budget preparations and pricing studies.

The extent to which standards are incorporated into the books of account, the points in the accounting process at which each standard is applied, the levels at which the standards are set, the frequency and appli-

COST AND MANAGEMENT

cation of revisions, and similar problems need answer in the individual case in terms of the uses to be made of the standards and their relative importance to the individual company.

Good judgment, with some luck and a sharp pencil, means much these days.

DETERMINING COSTS OF CLERICAL FUNCTIONS IN A SMALL OFFICE

John J. Ruster, in the N.A.C.A. bulletin, XXIX, No. 17, 1969, has written an article on costs in the small office. The facts mentioned are of interest to the sales department and to management generally. Office costs are common to the offices of larger organizations but the smaller offices receive little attention and are not often made subject to the elaborate surveys of methods involving job evaluation. While the executive officer may question the office expense, there is generally no concrete information available to stand as evidence for the need of current (and possibly increased) outlay. Nevertheless, with a few hours' work, basic data can be compiled which will be of incalculable value in assaying present performance, setting standards, and planning future operations.

While the detail cannot be defined it should be limited to the practical value of supporting the desired controlling information. Numbered documents make it possible to determine the volume of clerical work performed in any given period instantly by reference to the first and last number of any series of documents used during that period, such as invoices or credits issued, purchase orders, purchase vouchers, production orders, or cheques issued. The number of individual payments received during the period may be ascertained from the cash receipts record. The number of active accounts receivable and accounts payable should also be determined periodically, noting the number of accounts showing balances as well as the total number on the books.

For example, the cost of handling accounts receivable can therefore be measured by the number of sales invoices and credits issued, while the purchasing function can be measured by the number of purchase vouchers entered. Work sheets of clerical work hours and earnings can be prepared from the payroll records. Unit costs can be computed in man hours as well as in dollars. The man hour unit is perhaps the one to emphasize most as it serves to disclose the effect on costs of office functions of variations in salary rates and makes possible a comparison of the relative efficiency in different periods. To make such a comparison valid, the man hours considered should be the man hours worked, eliminating holidays, time lost, etc. In making such comparisons it is very important that each function be clearly defined and that the items be comparable.

An office survey may not be so exhaustive as to be scientifically exact in a laboratory sense, but being quickly assembled within limitations may still be of value as a basis for further study of methods in each department which appears to be operating at a high cost. At this time the benefit is almost individual since no general statistics have been accumulated to form a comparable standard office operation. Efficiency in the small office is a desirable contribution to the success of the business itself.

CURRENT LITERATURE DIGEST

SOME CURRENT PROBLEMS OF CONTROLLERSHIP

The Controller, XVI, 5, 236, reviews current problems in an article by Christian E. Jařchow. The topics studied include:

1. Uncertainties of the present business situation.
2. The rising fixed costs of business to-day.
3. Implications of rising fixed costs on break-even points.
4. Some observations on wages, prices, and profits.
5. Economic earnings versus monetary earnings.
6. Impact of rising price levels on corporate financial policy.

The comment under each of these headings is generally interesting. Some of the points which might be mentioned are in the following: There are some factors which seem to indicate that we may be coming closer to a period of recession than the immediate future indicates. No matter which course business may take in the future, there will always arise certain problems peculiar to that situation. Modern American business is particularly vulnerable if a recession should occur now. The term "break-even point" was almost unknown a few years ago. To-day industry is becoming increasingly conscious of its importance.

There is a growing recognition of the fact that increases in wages without corresponding increases in product prices can only come when there is a real offset to higher wage costs through gains in productivity — whether through better employee efficiency or through better methods.

While we are living in a period when there is much to be concerned about, on the contrary, there is much that is stimulating, and much that presents a real challenge. "The survival of the fittest" is not less true to-day.

PARAMOUNT KWIKSORT

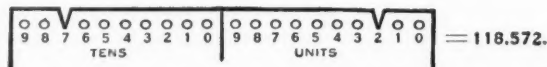
Paramount-Kwiksort system is a simple and inexpensive method of sorting and classifying all sorts of data from small job tickets, time cards and stores requisitions to the comprehensive analysis cards essential to the present day method of scientific management. Kwiksort was invented by an English accountant and its first application was made by the Copeland-Chatterson Company Limited, Stroud, Gloucester, England, in the distribution of work slips in one of the large rubber plants. Paramount-Kwiksort was introduced into Canada in 1928 by Copeland-Chatterson Limited, Brampton. Kwiksort as a device is the quickest sorting system and requires no machinery and very little equipment—a punch for slotting and a needle for sorting.

The cards are punched with a series of holes along the edge of the card. Each hole represents a definite value in the group or field allotted to a certain classification. The holes vary according to the number of classifications into which it is desired to assemble the cards and the particular hole or holes corresponding to the information to be indicated are slotted away to the edge of the card. The purpose of the sorting is to facilitate the recording of the information on the cards into the desired classifications.

The definite methods of coding are direct code, extended numerical

CURRENT LITERATURE DIGEST

code, the condensed code where only a limited space is available, also the alphabetical code. Along a 5" edge it is possible to code 99,999 positive and non-conflicting numerical classifications. Cards can be supplied from 2×3 to $8\frac{1}{2} \times 11$. There is actually no limitation to a card size depending of course on its practical application.



The 0-9 Code. The above illustrates the simplest form of numerical coding, called extended coding. A series of ten holes is allotted for units, tens, hundreds, thousands, until the desired limit is reached, each series bearing numbers 0 to 9 under the respective holes. The above illustrates slotting for 118,572. A complete numerical sequence is thus obtained with a minimum amount of slotting, but coding can be condensed if required.



When the amount of coding required is such that a large card would be required, the size of the card can be greatly reduced by adopting the 7, 4, 2, 1 or condensed code—see illustration.

Kwiksort cards are delivered to the purchaser with the holes around the edge unslotted. The holes are slotted by the user. Kwiksort cards are coded by numerical, alphabetical, geographical, chronological or direct according to the sorting desired.

The cards are coded and slotted only for sorting. The face or body of the card is printed and used as a regular record card or statistical record.

Sorting. The needle is the only tool or equipment needed for sorting. The Paramount cards when they arrive in the Analysis Department are usually in a mixed-up condition, some face up and some face down and in other positions in the stack. All cards must be right side up facing the operator. By inserting the sorting needle through the corner hole and lifting away, the projecting cards can be arranged in the correct position. Repeat this operation with the other corners until the cards are correctly positioned.

As a method it is the most economical way of securing accounting and statistical information. Slotting is easily and quickly done — sixty thousand cards an hour is not out of the way as a large number of cards fall away from the needle at each needling.

COST AND MANAGEMENT

NEW POST-WAR LIQUID TYPE **DUPLICATOR**

**DELIVERS TWICE AS MANY
COPIES PER MINUTE**



That's the performance record of the newest Ditto liquid-type duplicator. Incorporating improvements envisioned before the war, this latest addition to the Ditto line delivers up to 140 copies per minute, three hundred and more copies from each master, four colors in one operation of anything typed, handwritten, drawn or printed—without stencils, mats, or type. When this trim, modern duplicator is not in use, receiving tray may be folded over drum to protect vital mechanical parts from dust and damage. Improved liquid and pressure control gives you brighter, more legible copies; a sturdy reversible feed tray permits faster, easier handling of any size paper. And changing masters is surprisingly simple with the new type master clamp. All these important advantages of the new Ditto duplicator add up to substantial savings in time and money. Investigate now. Contact your local dealer or write direct.

DITTO

TRADE MARK REG. U. S. PAT. OFF.

**Investigate Ditto Payset, The Machineless
Payroll System for Small Businesses.
Write for Samples.**



DITTO of CANADA, Limited

310 Spadina Ave., Toronto, Ontario, Canada

Phone: Adelaide 1084

Report Writing

By A. E. CUTFORTH, C.B.E., F.C.A.,

(Copyright Gee & Co., Publishers, London, Eng.)

This paper is published in *Cost and Management* through the kind permission of the author, Sir Arthur Cutforth and the publishers, Gee & Co. While the paper has been prepared specifically for public accountants, these same principles could be well applied by industrial accountants in the presentation of reports to Management.

When one remembers what an important feature of a professional accountant's work Report writing is, it seems strange that no book on the subject has been written by an accountant for accountants. Nor, so far as I am aware, has any paper been read before this or kindred Students' Societies, if I except a most interesting paper delivered by Mr. B. H. Binder in April, 1922, before the Chartered Accountant Students Society of London on the wider subject, entitled "The Art of Presentation," which embraced, among several other matters, the writing of reports.

The reason for this absence of literature was not fully apparent to me until I began to prepare this paper. Report writing does not readily lend itself to being written about in a useful or practical way. One cannot dogmatise about reports in general or reduce report writing to an exact science. One cannot lay down precise rules to which all reports should conform. A man who writes a report must have collected and considered a certain number of facts, and the report is the tangible result of such collection and consideration. It reflects the writer's attitude of mind and processes of reasoning. It may be called, with some truth, an X-ray photograph of the writer's brain. To use the words of the Church of England Catechism, a good report may well be "The outward and visible sign of an inward and spiritual grace."

I realize that I could hardly expect to interest you this evening if I confined myself to generalities and ignored practical examples and suggestions. At the same time, I was anxious not to deal with the subject on too narrow lines, as this might lead you to think that its scope was limited, whereas I desire to suggest to you that it is very far-reaching indeed, and of equal interest to all of us. In framing my paper, I have endeavoured to effect a compromise between these two ideas.

I have prepared, and propose to hand out to each of you in a few minutes, three documents, and to go through them very briefly with you.

The first document is a letter of instructions to an accountant from his client asking him to make a certain investigation and to submit a report thereon.

The second is the report which the accountant proposes to submit, and which I suggest is imperfect in form and incomplete in substance. At the bottom of each page will be found noted the criticism I make on it.

The third is the report remodelled and elaborated, after giving effect to the criticisms.

But before I distribute these papers, I would like to submit to you some mottoes which I think you will find useful to bear in mind when you

REPORT WRITING

come to prepare a report, and I will make a few remarks on each. They are six in number:

- (1) Use your imagination.
- (2) Don't be "hustled."
- (3) Be simple.
- (4) Where practicable, collect and summarize your most important findings and conclusions.
- (5) Confirm the facts and information submitted in your report, so far as is possible.
- (6) Obtain, if possible, an independent opinion on your draft report.

MOTTO NO. 1

"Use Your Imagination"

We are often told that accountants should confine themselves to facts and steer clear of fancies. In one sense this is true enough; but an accountant without imagination is an accountant without judgment. An alternative motto might be: "Put yourself in the other man's place."

There is scope for your imagination from the time when you first begin your inquiry to the time when you complete your report. Visualize the position and the point of view of the people who are supplying you with the information on which you are to report—imagine whether they are disinterested in the matter or whether they may have any ulterior motives; imagine whether they are well equipped to form a judgment on the matters on which they give you their opinions; imagine whether any independent source exists from which you could confirm the correctness of the information they give you or the views they express.

Visualize also the position of the client to whom your report is to be addressed. Is he a man who understands accounts? If he is not, be careful to avoid technical accountancy terms or descriptions of bookkeeping entries; also, if you have to submit accounts, let these be as simple as possible in form and phraseology. Is your client a man having technical knowledge of the class of business on which you are reporting? If he is, then you may be able to supply him with details of a technical or special character which, though not very informing to you, may be of great interest and importance to him.

Talking of imagination reminds me of an occurrence in my student days. It is not very opposite to this lecture, except that it does illustrate how imagination may help and lack of imagination hinder even an embryo accountant. A young accountancy student was asked what first steps he would take on being instructed to audit the accounts of a distillery. He failed to appreciate the nature of the answer the examiner expected, and, as he came from a strong Quaker family, he wrote: "I should refuse, on principle, to have anything to do with the liquor trade in any form." I fear he was not awarded any marks for his answer. Another student in the same class was asked to say what special or characteristic item he would expect to find in the Balance Sheet of a Central African Plantation Company. He was serving his article in a very small office, and his experience was mainly confined to the preparation of accounts for small retail trades-

COST AND MANAGEMENT

men. But, being gifted with imagination, he replied that he would expect to find among the assets "stocks of elephants and slaves at or under cost of capture and taming." I have no doubt that the examiner suitably rewarded him.

MOTTO NO. 2

"Don't be 'Hustled'."

By this expression I do not suggest that the work of collecting information and preparing the report should proceed in a leisurely fashion. Indeed, it is very frequently the case that time is of the greatest value, and that you are pressed by your client to submit your report at the earliest possible moment. What I mean is: "Take time to consider carefully the scope and objects of your inquiry before you become immersed in the details." In other words: "Don't dash in among the trees till you have got a glimpse of the wood as a whole."

A great friend of mine, a Scottish Chartered Accountant, who had a very considerable experience of report writing, used to say, half-humorously, that he always wrote his report first and made his investigation afterwards. What he intended to convey was that, so far as was possible, he drafted in advance the form and general scheme of his report while his mind was still free from details and the main objects of the inquiry were fresh in his thoughts; and then, as his investigation progressed, he filled in the details, and, if circumstances so required, amended the form of the report.

If possible, do not send in your report the moment the last word is written. Put it away for a day if you can, and then, having slept over it, take it up and read it through again carefully and quietly. Things often look so very different in the cold light of the morning. Not infrequently you will find that the phraseology can be improved or paragraphs rearranged, or that points which have escaped you when you concentrated your attention on the writing of each paragraph become apparent when, after a short interval, you look at your handiwork as a whole.

MOTTO NO. 3

"Be Simple"

Some people are to be found who think that an important occasion demands the use of high-flown language. But high-sounding words and involved sentences do not deceive the wise, though they may impress the ignorant. An accountant who attempts to decorate his reports in this manner is nothing but a poseur, and frequently the only person who takes a poseur at his face value, is the poseur himself. You will remember, no doubt, Sir W. S. Gilbert's play, "Patience" in which the poetic poseur Bunthorne, talking of himself, gave expression to these lines:

"And everyone will say
As you walk your mystic way
'If this young man expresses himself in terms too deep for me,
Why, what a very cultivated kind of youth
This kind of youth must be.'
But, as you know, Bunthorne's audience only consisted of love-sick

REPORT WRITING

maidens, and even they turned against him in the end. The people who read our reports are made of sterner stuff, and they will not be deceived even temporarily, by such means.

So, at all costs, be simple. And the more complicated or involved the matter upon which you are reporting, the more must you strive after simplicity. Choose short words, in preference to long ones. Use short sentences. Avoid technical terms.

It is not always easy to make a report clear and intelligible in cases where a great deal of detail has necessarily to be dealt with. I remember finding myself in a difficulty of this character a number of years ago in connection with a report to be made to the directors of a very large undertaking recommending a system of Cost Accounting. No system of Cost Accounts was in operation; indeed, the business was not of a class in which a system of Cost Accounts is usually found. Furthermore, the system which I recommended embodied some quite unusual features. It was necessary that the company should be fully advised as to the detailed steps necessary to operate the system; but at the same time I realized that if the directors were to receive a very lengthy report, they might find considerable difficulty in visualizing clearly the general principles involved. I therefore addressed to the Board quite a short report, which was confined to an outline of the scheme in principle; but I submitted with the report a lengthy memorandum, setting out in detail all the steps to be taken to institute the Cost Accounting system. By this means the Board were able to consider the matter broadly and to come to a decision, while the memorandum was studied by the heads of the various departments who would be charged with the duty of working the system.

I merely mention this matter as an illustration of one of the many means by which a report can be simplified.

MOTTO NO. 4

"Where Practicable, Collect and Summarize Your Most Important Findings and Conclusions."

This motto calls for little explanation, but many a report has been spoiled by failure to observe it. Your comments or conclusions upon each of the various matters about which you are reporting will probably have to appear immediately after the respective paragraphs in which the facts are recited; indeed, it is logical that they should do so. But it may be very helpful to the client to find a summary of them in a concluding paragraph of the report; he can then carry them clearly in his mind, and can appreciate their relative importance.

I was making an investigation of some accounts not many months ago in connection with a case before the Courts. My clients, the plaintiffs, challenged the correctness of certain accounts of the defendants and my inquiries were directed to a number of specific points in such accounts. My report dealt in detail with each point, and was somewhat lengthy. In certain of the instances, I reported that the figures were incorrect; in other instances I had to advise that the correctness of the figures were open to doubt, as debatable points were involved; in other cases I stated that I

COST AND MANAGEMENT

could not verify the correctness of the figures, owing to the absence of full information; in other cases I reported that certain figures, though incorrect, did not appear to have any bearing on the particular matter in dispute; while in the remaining cases I was able to state definitely that the figures were correct.

My report was to be handed to counsel for the plaintiffs, and realizing this, I set out in the concluding paragraph a summary of the items I had queried, differentiating between—

- (a) Items which were incorrect;
 - (b) Items the correctness of which was debatable; and
 - (c) Items the correctness of which I was unable to prove or disprove;
- and also distinguishing between items which affected the matters in dispute and items which did not appear to do so.

You can appreciate that such a summary would be very helpful to a busy counsel. It would show him at a glance the points requiring to be considered, and he could, practically speaking, dismiss from his mind all other matters mentioned in the report.

MOTTO NO. 5

"Confirm the Facts and Information Submitted in Your Report, so Far as is Possible."

While you are naturally careful in collecting facts and figures for your report to see that they are accurate, it is very advisable, when you have rearranged and condensed them in the report itself, to have them independently checked in that form—assuming, of course, that you have the opportunity. This is especially important when the information may have been collected from more than one person, or where it comes to you verbally and not in writing, or where the persons giving the information may not be aware of the exact purpose for which it is required. I have known or heard of a number of cases where a report has been criticized, on the grounds that it did not present the facts accurately, when a precaution such as I have mentioned would have obviated this. We must realize, of course, that in a number of instances the parties supplying the information to us are not disinterested in the matter—for example, in cases where we investigate the accounts of a business on behalf of a prospective purchaser or investor. But even in these cases a great deal of the information summarized in the report can, without prejudicing the interests of our clients, be submitted to the persons best able to confirm its accuracy for their approval.

I remember a number of years ago investigating the head office accounts and records of a group of foreign railways on behalf of a firm of London financiers who had interested themselves in the public issues of the stocks of that group. In particular, my inquiries were directed to ascertaining the true net earnings accruing from the operation of the railway systems comprised in the group, and the destination of such earnings. The matter was very complicated, as there were a large number of interlocking companies, many of whom held each others stocks and bonds. The information was largely collected from a number of reports and returns

REPORT WRITING

received from abroad; and there were several debatable matters upon which more than one view could be held—e.g. the allocation of certain charges as between Capital and Revenue. The report, when completed, was a very lengthy document, and I was in considerable doubt as to whether in all respects the information contained in it was summarized correctly, seeing that it had been extracted from a very large mass of data. I realized that there was one man eminently fitted to express an opinion on the matter—namely, the London manager of the companies. I therefore took a carbon copy of the draft report, and merely cut out of it the opinions which I had expressed on the debatable points, and the general conclusions at which I had arrived; and I handed the draft report, in its mutilated form, to the London manager, knowing that, although he was a very fair-minded man, and believing that if I had made a mis-statement in favour of his companies he would point it out to me. As a result of this course, I was able to make some important and necessary modifications in the information given in the report without in any respect prejudicing my client's interests.

THE SIXTH AND LAST MOTTO IS

"Obtain, if Possible, an Independent Opinion on Your Draft Report."

I don't think I need dilate upon this motto. It is surprising how a sentence or a paragraph in a report may convey one impression to one person and quite another impression to another.

It often happens that an ambiguity may be entirely removed by the transposition of a few words or the addition or deletion of so small a thing as a comma. Therefore, if you have the opportunity, ask someone else in your office, whose opinion you value, to read through your draft report and tell you how it strikes him. What he has to say may well strike you!

My wife, who has a passion for solid literature, informed me the other night that she had read in some authoritative book—a publication, I presume, of the Royal Statistical Society—that it had been computed that no less than 80 per cent. of those husbands who have blue eyes desert their wives. I expressed some doubt on the subject, and asked her to refer again to the source of the information. This she did, and informed me the next evening with evident relief, that what the book said was that no less than 80 per cent. of those husbands who desert their wives have blue eyes. A very different proposition, and all due to the transposition of a few words.

In conclusion, I would like to address a few remarks to the younger students in particular.

Some of you may feel that the subject of my paper to-night is only of practical interest to the practicing accountant or to managing clerks, seeing that skilled investigations can as a rule only be carried through, and reports thereon prepared, by accountants of many years' experience. But I cannot too strongly urge upon even the youngest of you not to neglect, at the outset of his career, any opportunity of fostering the qualities which go to the making of a good report writer. It is more than probable that

(NOTE: The text of the book now includes examples of documents, criticisms and report which for sake of brevity are omitted here).

COST AND MANAGEMENT

for some years you may never take a hand in the writing of a report, and it may well happen that at no stage of your career will you be called upon to write reports with much frequency. But the qualities which you will develop will prove of the greatest service to you, no matter what the character of your work may be.

And what are the qualities to which I refer?

They include the habit of thinking logically; of expressing oneself, whether verbally or in writing, simply and clearly; of discriminating between what is important and what is trivial; of marshalling facts in proper order and sequence; of looking at problems from more than one angle; of seeking for independent confirmation of information one is asked to accept.

There is hardly one of these qualities for which each one of us has not daily use. They are the very foundations upon which our professional work is built.

And how can the younger students cultivate them?

Not, I fear, by studying text-books. And, indeed, if they could be acquired by this means, I should hesitate to recommend such a course, knowing well that the examinations for which you have to study during the period of your apprenticeship demand that all your "close" reading shall be confined to the subjects appearing in the examination syllabus. No; it is by other, and I think, less irksome means that these attributes may be developed.

Try to cultivate a taste for reading good English; eschew the more sensational newspapers, and make a practice of reading the leading and other general articles in the more sober and responsible of our daily journals. Read the verbatim reports of Parliamentary debates; also the reported speeches of well-read and well-informed men. I do not know whether many of you read at all carefully the memorandum addressed by this country a few years after the end of the war to its European Allies in connection with international indebtedness, and shortly referred to as the "Balfour Note." People may differ as to certain of its conclusions, or as to its expediency; but all, I think, agree that as an exposition of logical thought and clear language it was unsurpassed.

If you read weekly and monthly periodicals, do not let your attention be confined to magazines devoted to illustrated fiction; read also those publications in which well-written essays, reviews, and biographies are to be found.

It has been fashionable in recent years to say, "Can any good thing come out of Whitehall?" But there is one good thing which Whitehall has, for many years past, helped to produce. I refer to the reports of Committees set up by Parliament or by Government Departments, to make certain investigations and inquiries. These reports are, not infrequently, drafted by men in the higher ranks of the Civil Service; and in language and in general arrangement they are, in many cases, models of what good reports should be. A number of the reports are published, and can be procured from His Majesty's Stationery Office at cheap prices. They are well worth reading for the reasons which I have indicated above, quite apart from any interest in the particular subjects with which they deal.

REPORT WRITING

Then again, not a little can be done by you in your own offices. If you have a letter to write or to draft, take a little trouble over it, no matter how unimportant it may be in itself. Do not let any written production of yours pass from your hands that is loose in construction or faulty in grammar or punctuation. Find opportunities of reading carefully the carbon or press copies of the reports which go out from your own office, in the preparation of which you may have had no hand.

By all the above means,—both in and out of office hours—you will steadily though imperceptibly add to your powers of expression; you will strengthen your logical faculties; you will stimulate your powers of criticism; and, in time you will develop to a higher degree the many qualities that go to the making of a good accountant.

The Basis for Adequate Financial Reporting

Excerpts from an address by W. A. Paton, Professor of Accounting, School of Business Administration, University of Michigan, Ann Arbor, Mich., given before the 25th General Management Conference of the American Management Association.

The most objectionable and obstructive tradition of accounting is conservatism, so-called. Accountants generally, without fully understanding what they are doing, kowtow to this tradition. The textbooks make it a cardinal virtue, and the practicing accountant feels that any proposal seeking to broaden the horizon of accounting is effectively squelched if excuse can be found for referring to it as nonconservative.

Applying conservatism in accounting apparently means to most accountants on the one hand the understatement of assets by various means and on the other the understatement of net income. As has often been pointed out, these two practices are not always consistent. If, for example, the cost of acquiring a unit of depreciable property is charged to revenues in the year of acquisition the immediate results is understatement of assets and understatement of earnings, but in succeeding years—during the useful life of the property in question—one effect of the procedure will be to overstate income performance. Aside from the backlash of inconsistency, however, there is no substantive defense—practical or otherwise—for a policy of deliberate understating of any economic measurement in the business enterprise. There is no virtue in either understatement or overstatement. The interested parties want to know the facts of their undertaking as accurately as it is practicable to determine them. They don't want to be confused by an array of data that have been subjected to a process of paring down in varying and often undisclosed amounts.

Deliberate suppression of certain types of asset costs, in certain circumstances, has long been a feature of business accounting, supported in the name of conservatism. An outstanding example is found in the practice of charging to capital "surplus" the costs of organizing an enterprise and raising the necessary funds. A stockholder, for example, invests \$100 and under the authority of a state statute permitting part of this amount to be



National Mechanized Accounting

CUTS
COSTS
UP TO

30%

Hotels . . . department stores . . . banks . . . industrial offices . . . businesses of every type—all report savings in this range after *mechanizing* their accounting with National Accounting Machines. These savings often paid for the whole installation the first year—and then ran on indefinitely! Some of these concerns were large—some employed only 50 . . . Could *you* cut costs correspondingly? Ask your local National representative to check your present set-up, and report to you fully and *specifically*. There is no cost or obligation of any kind.

National

CASH REGISTERS
ACCOUNTING-BOOKKEEPING MACHINES

THE NATIONAL CASH REGISTER COMPANY
OF CANADA LIMITED
TORONTO

THE BASIS FOR ADEQUATE FINANCIAL REPORTING

described as paid-in surplus (incidentally a type of statute for which no reasonable justification exists) half of the investment is designated as stated capital and half as capital surplus. Then the organization and financing costs (legal fees, commissions, printing costs, etc.) amounting, for example, to \$5 are deducted from so-called capital surplus and the first balance sheet shows assets and stock equity of only \$95. This is the same thing as reporting to the stockholder that five per cent. of his investment has been lost in the process of bringing the enterprise into being.

Closely related to the policy of suppressing organizing and financing costs is the absorption of goodwill and other intangibles acquired by reducing the initial equity of the stockholder. Without attempting any discussion of the accounting problems associated with intangibles it may be pointed out that when intangibles having actual value are contributed by the investor, or when contributed funds are used to purchase intangibles, it is downright misstatement to fail to recognize such property in the accounts.

But omission of assets costs from the accounts is not confined to intangibles. Suppression of costs of building and equipment is common practice, and is generally defended as conservative accounting. We are all familiar with the fact that in many enterprises substantial amounts of true additions are charged directly to revenues as maintenance.

Recently I heard of a case where a company spent \$10,000 paving a parking lot and charged the entire cost to repairs. Similar examples are not hard to find.

The result of all such practices is persistent understatement of property to an indeterminate amount. That the amount is often substantial can hardly be doubted. The suppression of the cost of one waste basket isn't a very serious matter but it must not be forgotten that a multitude of small items may add up to a total of some consequence.

Closely allied to practices involving immediate suppression of assets is the policy of initial recognition followed by arbitrary, premature absorption. Before the days of stated value and capital surplus organization, financing, and development costs were commonly set up as deferred charges and writeoff was undertaken rapidly as soon as revenues appeared in substantial volume. The usual recommendation in the auditing textbooks was absorption in two or three years. In the case of goodwill and allied intangibles, likewise, it has long been common practice to write off the total cost as soon as this could be done without impairing the showing of income too seriously, without regard to the actual status of the assets.

With respect to tangible assets sentiment in favor of writeoff during a shorter period than the probable economic life of the property has not been so strong, although numerous cases of overdepreciation are found in practice.

Another questionable aspect of accounting practice, often resulting in substantial understatement of property, is the tendency to neglect to recognize assets acquired without cost, or assets having values substantially in excess of related costs. Important resources are sometimes acquired by gift, discovery (e.g., a mineral deposit), invention, and unexpected recovery (e.g., a plant in a foreign country previously treated as lost). It is usually agreed that property received through inheritance or donation should be

COST AND MANAGEMENT

recorded at fair market value as of date of acquisition and there is some support for the view that receivables, securities, and other property recovered after having been written off as worthless should be restored to the accounts in terms of recovered values. When it comes to assets acquired through exploration, invention, and development, however, prevailing opinion seems to be that accounting recognition is improper, except to the extent of costs incurred, even where the amount of cost is negligible by comparison with the value of the resulting property.

Assets originating through physical growth and reproduction—accretion—are likewise generally ignored by the accounting process. As a rule, indeed, not even the applicable costs are capitalized. The result is that the property accounts of nurseries, plantations, lumber companies, and related concerns are often not worth the paper they are written on. Not long ago an important corporation, operating numerous tracts of timber on a continuing production basis, sold a relatively small part of its holdings for more than the remaining book value of all tracts owned.

The foregoing discussion boils down to a plea for complete disclosure, at significant figures, of the total assets of the business enterprise, as opposed to current policies of omission, premature absorption, and understatement in varying degree. A major reason for urging reform in this direction is the danger at the present time to property rights, and the institution of private enterprise itself, in persistent misstatement of existing assets.

Regulations of business—outside the utility field—has proceeded apace and that the concepts of "fair price" and "fair return" are becoming more and more potent in business generally, in wage disputes, and in other connections. In other words, the matter of earning rates, always intrinsically important to managers and owners, has become one of wide public interest. Now, what does substantial understatement of resources employed do to a computed earning rate? The effect, obviously, is a more or less serious understatement of earning power. At the present time, it is safe to say, most calculated rates of return based on accounting data are substantially in excess of the returns actually being earned. This is not a good situation, either from the standpoint of the parties immediately interested or from the standpoint of the relation of private enterprise to employees, consumers, government, or the general public.

Interest in earning rates is likely to wax rather than wane, and this is not in itself unreasonable or undesirable. Earning power is perhaps the outstanding fact of any business enterprise. But present accounting data are not satisfactory in this connection and present accounting methods require improvement if reliable, significant data regarding rates of return for business concerns are to be made available. As has been pointed out many times in recent years, people generally have rather wild ideas about business earnings. It has also often been pointed out that popular sentiment unfavorable to private enterprise is often largely founded on misconceptions and inaccurate data. In the light of these considerations the accountant needs to become more alive to his obligations to business and to the community, and he should undertake to improve his procedures, and abandon unsound conventions without delay.

The Balance Sheet From the Banker's Viewpoint

By R. L. BAILEY,
Manager, Bank of Montreal, Calgary

A Banker's life is a bit contradictory. After a loan is made he wonders if he will get his money back: After the loan is paid he then wonders how he is again going to place the funds at work. You, as accountants, are watch-dogs for your Company or employer. We, in turn, are watch-dogs for the deposits entrusted to our care. I would like to stress that point. We are largely custodians, not owners of our merchandise—which is money. Think how distressed you would be if you asked for your savings deposit in cash and received the reply, "We are sorry, we loaned your balance to John Blank for thirty days and, while the thirty days have long since passed, he has not yet paid it back." Admittedly, that may be an extreme example, but the theory is hammered into us very early in our banking life, and it is only natural, therefore, that we view a balance sheet, except our own of course, from a different angle than the customer. After one is satisfied as to the integrity and business ability of the borrower, the business properly capitalized, and that the money is required for ordinary business purposes, we look to the balance sheet supported by Profit and Loss and Surplus Accounts statements. Actually, we prefer to have at least three consecutive years' statements which we set up on a comparative form which shows at a glance the following important features:

- (a) Ratio of Current liabilities to Liquid Assets and the upward or downward trend of working capital for the period.
- (b) Movements in Inventory, Receivables and Turnover. If turnover has fallen off and liquids have remained stationary, there is obviously something wrong.
- (c) Movements in Bank Advances and Liabilities to others. For example, if merchandise and receivables show a sharp decline and the Bank loan remains stationary, we would at once enquire where the funds were going, and why.
- (d) Results of operations, profits or losses, and, if any dividends declared, or paid, if it was justified.

What engenders confidence most is what is accomplished over the years in good times and bad. If a killing is made in one year that is all to the good, but it has been our experience that when such a happy happening occurs it is usually more good luck than good management, and easy profits are sometimes dissipated.

I remember once telling an undertaker that he was withdrawing from his firm far more money than its earnings justified and in this he agreed, but he said that in 1918 the situation was approximately the same and the flu epidemic of that time had put him on his feet—what we need is another epidemic.

Speaking of sordid things, one feature I might mention here is whether or not a borrower is a one-man outfit. I do not necessarily mean—indi-

COST AND MANAGEMENT

vidually owned or controlled—but does the successful operation depend on one man or is somebody being trained to carry on in case of need.

I will not dwell on the liability side of the balance sheet—suffice it to say, if all liabilities are disclosed, proper provision made for accrued wages, taxes, et cetera, and contingent liabilities, if any, are shown—such as an endorser or guarantee furnished others—there are the debts that must be paid and for which banking assistance is required pending profits from future sales. Naturally, for this revenue we look to the liquid assets—merchandise, receivables, cash in the Bank and on hand—excluding any I.O.U.'s that might be in the petty cash box pending repayment from future salary cheques, and other liquids such as readily marketable stocks and bonds.

Merchandise is one of the most important items in the balance sheet and upon its proper valuation and its relation to the volume of sales depends, on a large measure, the way the business is directed. It is necessary for us to determine how the inventory is valued and if stock-taking is in competent hands. We prefer the stocks to be valued at the lower of cost or market. Some concerns value the stock at selling prices which, is unsound practice and should be discouraged. Is the stock well assorted, clean up-to-date and free from items hard to move at any price? Is adequate fire insurance carried?

Each business, of course, is to be considered in relation to its nature. For instance, in the wholesale grocery line inventory should turn over much more rapidly than in the wholesale hardware trade and as a consequence smaller inventories can be carried in the former than in the latter class. If merchandise is increasing without a corresponding increase in sales, the Company is either overstocked or speculating, and in the latter event this should be checked as it frequently involves heavy losses in the event of a reversal in the trend of price levels. Are out of date or slow moving lines properly written down?

RECEIVABLES

I include here both Accounts and Bills Receivable because the same remarks apply to both. The total of both these items must be in proper relation to the turnover according to the nature of the business and usual terms on which sales are made in the trade line. For instance—for goods sold on a 30-day basis, receivables theoretically should be about 1/12th of the total sales, and while it seldom happens that the ratio is as close as that, wide variance indicates that the usual terms are not followed or that the Receivables contain a lot of slow and weak accounts. Are the risks well spread? Obviously, from our point of view, it is often preferable to have ten \$10.00 accounts assigned to us than one \$100.00. Naturally, such an important asset requires careful examination and it is customary for the banks to ask for detailed lists of all accounts over a certain minimum. These lists are checked by us in various ways, not only to satisfy ourselves that credit is granted carefully, but to see that sales are not being pushed to increase volume. Some Accountants include an analysis of receivables in their statements and qualify the accounts according to the item outstanding—that is, accounts within 30, 60, 90 and 120 days show the per-

THE BALANCE SHEET FROM THE BANKER'S VIEWPOINT

centage each category bears to the total receivables. Such an analysis is particularly helpful to us as it shows at a glance not only the quality of the accounts but also the velocity of the collections. Collection of accounts is an important factor, and it is our opinion that as many accounts as possible should be converted into Bills Receivable as it provides an acknowledgment of the debt, a definite date for payment and puts the Company in possession of collateral which can, if need be, be used to obtain Bank credit. Moreover, collection is facilitated and payments can be closely followed. It is perhaps needless to say that only bona fide trade transactions should be included under these headings, and that accounts which are obviously tied up and weak should receive special attention by putting them on a liquidation basis and further sales made only on a cash basis. We would suggest that these should be classified, particularly if no reserve has been set up, as deferred receivables, and not included in liquid assets. It is sometimes found that included in the liquid receivables are accounts due by directors or employees. These should not be permitted—the accounts should be segregated and shown separately amongst the deferred or slow assets as they are seldom readily recoverable. This also applies to accounts due by subsidiary companies which would require full explanation as to the nature of such advances, source of, and probable date of repayment. Annual increase or decrease in total receivables should be reflected elsewhere in the balance sheet if they are in regular order. Increases should only be due to an increase in the volume of sales, while decreases, unless reflected in a corresponding reduction in liabilities, would appear to indicate that the business is either being wound up or is drying up.

My remarks under these two headings apply to normal times. It is appreciated that during the war it was necessary to take not what you wanted to buy but what you could get. Stocks were often out of proportion to sales volume and were not well assorted or well made—but these were abnormal times. Things are creeping back to normal and, if past experience teaches us anything, now is the time to get the merchandise shelves in order. Credit men too, and I include myself, had during the war years more or less of a holiday. When demand exceeds supply the retailers will see that their wholesale accounts are well paid—they know full well if they do not pay they will lose whatever quota standings they have with their suppliers, and will soon find themselves without anything to sell. Let supply exceed demand, however, and the trend is altogether different. So just because we avoided credit losses during the past few years don't let us get an exaggerated opinion of our credit judgment. Let us remember it is when times are good that bad debts are placed on the books.

Other liquids such as cash and investments in stocks and bonds require little comment; all we do here is ascertain if the investments are readily marketable and are investments—not gambles, if the securities are properly valued in the balance sheet—sometimes the purchase price is used irrespective of present day valuations which may be good or bad depending on whether the market for the security is strong or weak.

Time does not permit discussing Fixed Assets, but again from a banker's point of view, no particular attention is paid to these assets as a basis for

COST AND MANAGEMENT

loans for current operations. Providing the premises are suitable, in good repair and properly located for their purpose, the cost of the building is in keeping with the requirements of the business and proper insurance coverage carried, we have little further interest. If there is a mortgage or the property is leasehold, we should know if mortgage payments, plus interest, are up to date or that the lease is of sufficient duration to permit continuous operations. Naturally our interest in fixed assets increases as the possibility of repayment of our advances from liquid assets decreases.

Accounts Payable Procedures

By JAMES MITCHELL,

The Robert Simpson Co. Ltd., Toronto, Ont.

DEFINITION

The recording and accounting for liability to others for material and services purchased, and the provision for and payment thereof.

As part of the establishment of a procedure to accomplish effective control, consideration must be given to the functions of purchasing, receiving, recording and paying.

PURCHASING

Purchase orders are written showing number, date, name and address of Supplier, description of materials or services including quantity and price, delivery date, shipping instructions and terms of purchase.

The original of purchase order is sent to the supplier and if accepted becomes a contract to supply the material or services in accordance with the terms stated in the order.

RECEIVING

On arrival of goods from suppliers, a receiving report is prepared showing name and address of supplier, description of goods, date received and purchase order number.

These receiving reports are usually prepared in sufficient copies to provide for use of:

- Department receiving the goods,
- Purchasing Department, to be matched with invoice and
- Receiving Department, as permanent record.

RECORDING

Wide variations in systems arise at this point due to individual requirements. This discussion, therefore, will be limited to basic requirements for effective control. Receipt of invoice and merchandise becomes a liability and provision must be made for invoice approval and recording, with plans for immediate or deferred payment according to terms of purchase.

ACCOUNTS PAYABLE PROCEDURES

Recording of invoices is made in the Voucher Register, Purchase Journal or Accounts Payable ledger showing reference number, vendor's name and address, amount of invoice and terms. Distribution of the charges is made in purchase journal or voucher register after which documents are filed.

PAYING

As invoices become due and payable, cheques are prepared and mailed to suppliers, thus completing the contracts. Remittance statements usually accompany cheques showing the make-up of the settlement such as invoice dates, and amounts, cash discount and prepayment interest and net amount remitted.

* * *

Many variations can be found in Accounts Payable procedures, yet every plan or system must abide by these basic requirements to provide effective and accurate control records.

Briefly summarized, the following six definite steps constitute the basic requirements of an Accounts Payable System.

1. Purchase Order.
2. Receiving Report.
3. Approval of Invoices.
4. Recording in Purchase Journal or Voucher Register.
5. Issuance of Cheques.
6. Recording of Payment in Cheque Register.

In every step of this procedure full cognizance of the fact that the company's funds are involved, should be uppermost in the performance of each task: Frequently in small companies, one individual performs every step in the procedure, providing ineffective control. Where possible, it is imperative that the various steps be divided, thereby creating an internal check in each transaction.

SYSTEMS IN USE TO-DAY

There are two and possibly three main systems in use generally viz:

1. Voucher System.
2. Ledger System and the
3. Punched Card System.

Let us consider briefly the functions of these three systems with some of their advantages and possible disadvantages.

The Voucher System involves the placing of approved invoices in jackets or covers. A separate jacket is used for each supplier and the outside cover usually shows: vendor's name and address, a listing of the invoices inside, terms of purchase, number, and a distribution of the charges. These jackets are entered numerically in the voucher register which register at the end of a period, becomes a posting medium of a credit to the General ledger Accounts Payable Control Account and a debit to the various material and expense accounts. Vouchers or jackets are then filled chronologically by due date in an Unpaid Vouchers File. As the due dates approach, vouchers are removed for payment and after payment they are filed numerically or alphabetically in the Paid Vouchers File.

COST AND MANAGEMENT

ADVANTAGES

The Voucher System is simple and flexible making it an ideal system for any company regardless of size. Its easy balancing feature, freedom from tag-ends and the facility of compact filing make it the most desirable from every standpoint except historical.

DISADVANTAGES

In normal times, when the demand by purchasing agents, Department Managers and executives for historical information about purchases and suppliers is negligible, the voucher system fills the bill admirably. However, during the war years and even to-day historical information is frequently required for various reasons such as:

1. Ammunition for buyers in respect to volume of business done over a period of years with certain suppliers, used by them as a basis for obtaining fair quotas of merchandise.
2. Information on certain suppliers' dealings required for income tax and sales tax inspectors in alleged falsifications.
3. Volume of purchases by districts to offset prejudice against opening of stores in certain localities.
4. Statistics on cash discounts obtained in certain periods and on certain lines of goods.

It will be evident that to secure such information under the voucher system would require the removal from files of possibly hundreds of vouchers and while such studies are a chore under any system, the information is much more readily obtained under the ledger system.

LEDGER SYSTEM

This Ledger System comprises a ledger sheet for each supplier on which is posted the—invoice date, number and amount, the terms of purchase and the department charged with the goods.

In small businesses this is done by hand but in most reasonably large firms it is performed mechanically by some standard posting machine. Invoices after approval and distribution are controlled to the billing machine operators periodically and posted to the respective suppliers accounts. Ledger sheets are arranged alphabetically in trays and as postings are made, sheets are offset for review by persons responsible for paying. At the completion of each posting the offset sheets are reviewed for immediate payments or near future payments. Invoices due are written up on remittance statements at once and cheques requisitioned. Those due in the near future are also written up immediately and held by payers until due dates.

As invoices are paid, the items on the ledger sheet are keyed off with a symbol to prevent the danger of their being paid again.

From the duplicate copy of the cheque register the debit postings are made to the suppliers' accounts, thus clearing the ledger.

At each posting the billing machine operator first picks up the present ledger balance and after the posting on any account is completed, the machine automatically throws out the new balance.

Monthly trial balances are run off which tie in with the General Ledger Control Account.

ACCOUNTS PAYABLE PROCEDURES

ADVANTAGES

As pointed out previously, the main advantage of the ledger system is the comparative ease by which historical information can be obtained. When studies are required, all that is necessary is to refer to the ledger sheet of the suppliers under review. As sheets become filled they are removed from current trays and placed in transfer cases or binders, so that to obtain data covering a period of years there are only the two places to look. All sheets are filed alphabetically in both current and transfer ledgers.

DISADVANTAGES

The danger of postings to wrong accounts resulting in incorrect payments is a disadvantage of this system. These improper payments are sometimes difficult to recover from insecure or irresponsible suppliers—sometimes never recovered.

Other disadvantages are the feature of trial balance taking with its usual waste time in running down machine operators' errors; and the tag-ends that usually accumulate in any ledger system.

The former may be minimized by the selection of competent operators and training them properly, and the latter by periodic review of ledgers. Both factors can be greatly improved by efficient supervision.

PUNCHED CARD METHOD

This method of recording and paying Accounts Payable involves the punching of a card for each invoice, showing all the essential information for tabulation. After cards are punched and verified as to correctness they form a very valuable record that can be transcribed into all the paying, distribution, statistical and historical information that could be required, dependent, of course, on the information first punched into the card. These cards can be very speedily sorted into any desired groups such as due date, classification of merchandise, vendor, locality, etc. They can be transcribed on a printing machine to give visual records of all information punched into the cards originally such as: Cash discounts, freight, duty and distribution of charges to material and expense accounts. Settlement cheques and remittance statements are also printed from cards by printing machines.

From the standpoint of clean, efficient records which are capable of producing information quickly, it is difficult to comprehend any other system that can begin to compare with the Punched Card Method. Cards can be listed to form permanent printed records and even Summary Cards may be prepared from several detail cards to record total invoices by suppliers for any given period. This feature itself eliminates the necessity of keeping thousands of cards which would otherwise require considerable storage space.

DISADVANTAGES

Like any other system contemplated for Accounts Payable, cost of operation, which includes cost of equipment, must be considered and this factor demands careful thought when considering the punched card System.

COST AND MANAGEMENT

It is difficult to appreciate this system in use for Accounts Payable alone, in any business, no matter how large, on account of the comparatively higher cost for this one operation, over other equipment. Where it is employed on Accounts Payable, it is usually also used by the same company for other functions of the business such as, Accounts Receivable, Payrolls, Inventory records, Purchase reports, Sales Analysis and many others.

ORGANIZATION AND FUNCTION OF AN ACCOUNTS PAYABLE DEPARTMENT (Under the Ledger System)

We have already observed that in every step of Accounts Payable procedures, full cognizance of the fact that the Company's Funds are involved must be uppermost at all times. With this factor firmly in mind the Accounts Payable Department should be so organized that only indirect access may be had to the other basic factors of Accounts Payable such as Purchasing and Receiving records.

The Accounts Payable Department of a large organization is usually divided into four sections—Billing, Paying, Adjusting and correspondence.

BILLING

It is the function of the Billing Section to post invoices, debits, journal vouchers, cheques, etc., from these documents and balance to pre-determined controls prepared by another department of the general office organization. Since each individual posting is balanced, it might seem paradoxical to anticipate difficulty in balancing ledgers. Yet such, unfortunately, is the case; caused by operators picking up previous balances incorrectly, failure to properly make corrections after errors are discovered and ledger sheets being out of the tray at trial balance time. It should be the responsibility of the Supervisor to so train his billing staff that the importance of accurate billing and the danger and annoyances of incorrect billing are considered as of paramount importance in their daily work.

PAYING

The payers prime function is to requisition cheques daily to settle promptly and accurately the Company's accounts payable liabilities. Full advantage must be taken of all cash discounts offered, as well as prepayment interest on such accounts as are subject to this deduction for payment before maturity. Ledger sheets must be reviewed after each credit posting, prompt settlements made for accounts due and sheets inset for accounts which are to receive future attention.

Where the volume of ten day accounts is heavy, it is decidedly advantageous to have arrangements with suppliers for settlements on certain scheduled dates, and in most cases application by the Accounts Payable Department for this privilege is granted. For example: To correctly settle an account with ten day terms on which invoices are received daily would require cheques every day. Obviously this is costly as well as a tremendous amount of clerical work. Scheduled payments mean that certain definite

ACCOUNTS PAYABLE PROCEDURES

settlement dates are established when invoices for a given period will be paid. The most common is 5th and 20th—all invoices dated from the first to fifteenth of the month are paid on the 20th and invoices dated from the 16th to end of month are paid on the 5th following. It will be apparent that the average time taken on ten day invoices is $12\frac{1}{2}$ days which is inconsequential when considered in the light of saving in clerical work and in cost of the extra cheques themselves. Similar payment dates are scheduled for other accounts with varying terms.

Each payer is provided with schedules applicable to this own set of ledgers. These are headed up, one for each key payment date, showing name of vendors whose accounts are to be settled on these dates. Each sheet has 12 columns for the months of the year and as payments are made, a check mark is made against the supplier's name in the appropriate month column.

At the close of each day, payers complete the "Payers Daily Report," showing number of settlements made, scheduled payments completed and other duties applicable to their accounts. These are transcribed to a Master Control Sheet thus keeping the Supervisor informed on the progress of current work.

This Master Control is a good barometer of a payer's ability to keep his accounts settled on time.

Vendors' statements of account are a valuable aid to correct paying and reconciling. They are used wherever possible in place of company remittance forms and are returned to suppliers with cheques attached. It is desirable to obtain these statements of account and vendors should be encouraged to send them. They provide a reasonable assurance that company records are in agreement with suppliers and also give leads on items that might have gone astray and on which tracers may be started.

Unfortunately during the past few years, and probably due to inefficient and insufficient staff, some firms records leave much to be desired. No statements have been sent, payments have been merely credited in bulk without reference to details, all with resultant chaos. Occasionally, through the efforts of some enterprising new blood, the awakening arrives. Requests are made for a transcript of records sometimes over a period of years. At times letters are received which bring to our attention allegedly unpaid items in 1946, 1945 and even before. All such instances are troublesome and annoying and involve searching through archives. Such instances as these justify a continuous drive to obtain regular statements of account. In businesses with numerous suppliers to serve, cases like these commend the ledger system over the voucher system.

ADJUSTING

The adjusting section is responsible for requesting necessary adjustments on invoices, debits, vendors' credit notes and even the actual paying of very large accounts. These large accounts sometimes take from a couple of hours to half a day each to check off with statements and reconcile, and if left to the paying section would seriously retard the payment of other accounts less difficult to handle. The adjusters are paternal godfathers to

COST AND MANAGEMENT

the payers when difficulties arise. Being graduate payers they are equipped by experience and training to bring about speedy solutions to payers' daily problems.

CORRESPONDENCE

It has been estimated that 95% of all correspondence flowing through the Accounts Payable Department is due to errors made by suppliers and the company itself. An examination of letters over a period proves this to be true. All incoming mail should be reviewed by the Supervisor before passing to the Correspondence Section. In this way the supervisor has his finger on the pulse of his Department and in fact, his Company as a whole in the eyes of suppliers, in regard to Accounts Payable matters. Complaints of a moderately serious nature should be attended to by the Supervisor personally. Outgoing correspondence is of sufficient importance to justify at the very least, a periodic review by the Supervisor.

* * *

Other incidental features in the daily life of an Accounts Payable Department include:

ASSIGNMENTS

These are notifications, usually from banks, that your suppliers have assigned their interests in your account to banks, and settlement must be made direct to the banks. The notification of such assignments on ledger sheets under the ledger system of Accounts Payable is most convenient.

AUTHORIZATION OF CREDIT

Claims against suppliers for merchandise returns and shortages and price adjustments are first referred to the Accounts Payable Department for credit O.K. Notation is made on the ledger sheet and deduction effected in next settlement.

COLLECTION OF DEBIT BALANCES

These cover debit memos issued after payments are made on suppliers' accounts where no further offsetting credits are in prospect. These balances are Accounts Payable in name but Accounts Receivable in fact and are treated as such. Regular statements are sent to these vendors followed by the usual collection letters.

STATISTICS

The records of ratios of cash discounts, prepayment interest, and even daily payments to total purchases, if maintained continuously, are a solid foundation on which to forecast future expectations on these items. Budgeted Purchases first being determined, it is then only a matter of applying actual past ratios to these figures to produce a reasonably accurate forecast of future expectations to the Finance Department.

VENDOR-BUYER RELATIONSHIPS

It is important in all Accounts Payable dealings, and particularly in times like these, with many lines still in short supply, to help maintain a

ACCOUNTS PAYABLE PROCEDURES

cordial and co-operative vendor-buyer relationship. This, the Accounts Payable Department can do by close contact with both in matters of settlements and adjustments.

PUBLIC RELATIONS

A real opportunity is afforded the Accounts Payable Supervisor to cultivate goodwill by direct contact with suppliers, who, in the Department Store Business at least, may also be his Company's customers. A policy of frankness and fair dealing should be adopted. If errors are discovered in suppliers' invoices whether overcharges or undercharges, adjustments should be made promptly and with just as prompt notification to the suppliers of action taken. Goodwill may be acquired through the payment of Accounts strictly in accordance with terms of purchase. The practice of replying promptly to suppliers' correspondence is important in developing and maintaining goodwill. The policy on which department stores have thrived viz: "The customer is always right" may be applied, perhaps to a lesser degree in all business relations to foster and maintain good Public Relations.

SUPERVISION, TRAINING AND PERSONNEL

Proper supervision is the keynote in the success of any Accounts Payable Department or in fact any department. In these trying days of job—plentifullness, high labor turnover and staff indifference the lot of the supervisor is sometimes as unhappy one. Nevertheless, he must set the example by being on the job on time, by pitching in and actually doing the detail work when necessary, and by constant checking to see that verbal and written instructions are carried out.

For new employees a manual of Accounts Payable instructions should be available. This manual in addition to affording a source of authentic information, provides valuable training material as a text or reference book.

Written instructions, explaining the work in detail, for purposes of training and future reference, are invaluable. New employees especially can be very uncomfortable if the supervisor or instructor crowds them with more verbal detailed instruction than they can possibly digest at one time. If the procedure to be followed is laid down in writing, they will feel greater security and confidence and there will be no excuse for deviating from Standard practice.

During the interviewing of prospective employees a concise explanation of Company Policy should be given, including benefits: and a more detailed explanation of the particular job that is vacant. At this point the prospect should be asked if he is interested in the position offered and if he feels confident in fulfilling the requirements laid down. If sufficient time is taken in the interview much of the costly training period might be saved instead of wasted, should the new employee suddenly vanish after a trial period.

A supervisor should keep in mind that new people particularly are likely to be wondering how they are getting along—whether they are doing sufficiently well to be retained after a trial period. Especially the High

COST AND MANAGEMENT

School crop, new in business, will have no criteria by which to measure their own performances. Too often they are left to assume that they must be O.K. because they have not been told to the contrary. This is a mistake. Positive information about their progress should be given from time to time. Opportunity is offered the supervisor at the same time, to point out ways in which they might improve.

